No. 3994

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

H. ALLEN RISPIN,
Plaintiff in Error,

vs.

THE MIDNIGHT OIL COMPANY
(a corporation),
Defendant in Error.

CLOSING BRIEF FOR PLAINTIFF IN ERROR.

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CLOSING BRIEF FOR PLAINTIFF IN ERROR.

In reply to the able Brief for Defendant in Error, plaintiff in error makes the following points:

I. The discharge from liability of the Associated Oil Company, discharged plaintiff in error.

II. Although some authorities indicate that a complaint for liquidated damages need not allege the amount of actual damage, they do not go so far as to dispense with proof of some damage where it is alleged in the answer that no damage occurred.

III. The allegation contained in the answer, that the Associated Oil Company was barred by unavoidable delays, constitutes a defense to the cause of action pleaded.

IV. Plaintiff in error is entitled to have the propriety of liquidated damages tried as an issue of fact.

V. The contract in this case provides for a penalty and not for liquidated damages. A guaranty is always penal and cannot provide for liquidated damages.

VI. Conclusion.

The above arrangement of points does not follow the argument in the Brief for Defendant in Error, but we deem it the more logical order because until Point I, supra, is first disposed of, the other points are not even involved in the case. That is to say, plaintiff in error deems that the judgment should be reversed with directions to enter judgment in favor of plaintiff in error, on Point I, supra, and that the court will even find it unnecessary to pass on the remaining points.

I. THE DISCHARGE FROM LIABILITY OF THE ASSOCIATED OIL CO. DISCHARGED PLAINTIFF IN ERROR.

Defendant in error has three answers to our first proposition, viz.:

(a) The contract sued upon is not a guaranty;

(b) Admitting that the Associated Oil Company was prevented from drilling the well because it was not put into possession of the land by its lessors, still plaintiff in error was not thereby discharged because defendant in error was not obligated to deliver possession to the Associated;

(c) Performance by the Associated was prevented by strangers to the contract, and hence the failure to perform is not excusable.

Plaintiff in error replies to these answers as follows:

A. "The Contract Sued Upon Is Not a Guaranty."

Learned opposing counsel in his brief states (Brief for Defendant in Error, p. 18):

> "It is plain to be seen that this agreement is absolutely independent of any agreement which the Associated Oil Company had with the Hopewell Oil Company; and that it in no manner purports to guarantee the performance of that contract."

We respectfully refer the court to the instrument itself (Trans. Rec., pp. 2-4).

The third recital contained in the instrument expressly refers to the contract between the Hopewell Oil Company and the Associated Oil Company, showing clearly that the parties were contracting expressly in reference to it.

The fourth recital states the obligation of the Associated Oil Company *in the exact language* of the contract between the Associated and the Hopewell.

The agreement itself expressly recites:

> " * * * the undersigned [plaintiff in error] hereby *guarantees* that the said Associated Oil Company, or its assigns, will drill * * * "

and then follows the language of the agreement *in the exact words and punctuation of the Hopewell-Associated agreement.*

We submit that there is absolutely no distinction possible between the contract executed by plaintiff in error and the common, ordinary, everyday contract signed by a surety company which guarantees the performance of work by a contractor in erecting a building or doing public work.

B. "Admitting that the Associated Oil Co. Was Prevented from Drilling the Well Because It Was Not Put Into Possession of the Land by Its Lessors, Still Plaintiff in Error Was Not Thereby Discharged Because Defendant in Error Was Not Obligated to Deliver Possession to the Associated."

The conclusion urged depends upon two premises, first, that defendant in error was not obligated to deliver possession, and second, that if defendant in error was not thus obligated, plaintiff in error was not discharged. Both premises are false, so the conclusion falls to the ground.

Taking up first the question of the liability of defendant in error to deliver possession, these are

the facts: The Hopewell Oil Company had an oil lease from the Western States Oil and Land Co. covering the lands described in the guaranty sued upon as well as other lands (Trans. Rec. p. 8). The Hopewell Oil Company entered into a contract with the Associated Oil Co. to develop said lands (Trans. Rec. pp. 19-26); the first provision of said contract was as follows (Trans. Rec. p. 20):

> "1. The said party of the first part [The Hopewell Oil Company] shall immediately deliver possession of said lands to the party of the second part [Associated Oil Co.] for operation under the terms of said lease, and under the terms of this agreement."

Said contract also provided as follows (Trans. Rec. p. 24):

> "9. The provisions, conditions, covenants and agreements herein contained shall inure to the benefit of *and be binding upon* the successors and assigns of the parties hereto."

The Hopewell Oil Company then assigned part of the lands covered by its lease from The Western States Oil and Land Company and also covered by its agreement with the Associated Oil Company to defendant in error; this assignment was an instrument in writing, executed by both parties thereto, and set forth in full in the record (Trans. Rec. pp. 26-30); this assignment expressly recited (Trans. Rec. pp. 27-28):

> "To Have and to Hold by the said The Midnight Oil Co. [defendant in error], its successors

> and assigns, subject, however, to all the terms, conditions, agreements, covenants and royalties expressed in said lease, which said terms, conditions, agreements, covenants and royalties The Midnight Oil Company agrees to keep, perform and pay so far as it relates the above described land assigned to it *and subject to the said operating contract as to all of the terms, conditions, agreements and covenants therein contained.*"

The assignment also expressly recited (Trans. Rec. p. 27):

> "*the purpose of this agreement being to subdivide both said lease and the said operating contract as above set forth.*"

The operating agreement expressly provided that it should be binding upon the successors and assigns of the parties; defendant in error joined with The Hopewell Oil Company in expressly reciting that it was their intention "to subdivide said lease and the said operating contract"; the assignment expressly provided that it was subject to all of the terms, conditions, agreements and covenants of the operating contract, and yet defendant in error says it was not bound to deliver possession of the land to the Associated.

It is obvious that defendant in error and the Hopewell Oil Company intended to, and actually did, subdivide the land, lease and operating contract so that each should have the benefit accruing from its portion and be subject to all the burdens appertaining to the same. They could not have expressed

this intent in more positive or appropriate language than they did.

If there is nothing in the record to indicate that defendant in error ever had possession of the land, neither is there anything to indicate that the Hopewell Oil Company ever did either. It was that part of the land assigned to defendant in error which the Associated was to commence drilling upon (Trans. Rec. p. 3). The uncertain condition of the title was clearly present to everyone's mind, as is attested by paragraph 6 of the Hopewell-Associated agreement (Trans. Rec. p. 23). It is inconceivable that the Hopewell Oil Co. intended that it should be liable to deliver possession to the Associated when it had disabled itself from so doing by assigning to defendant in error. According to learned counsel's views the defendant in error might have sublet this land to say the Standard Oil Co. and then have sued plaintiff in error because the Associated did not drill.

We, therefore, submit that defendant in error clearly rendered performance by the Associated Oil Company impossible by its own default, and that this case very clearly comes under the authorities cited in our opening brief.

But it is not even necessary to examine and construe these different instruments in order to dispose of learned counsel's argument. His argument assumes that it is only where a principal obligor is

relieved by default of the obligee, that the guarantor is discharged. There is no such qualification to the rule. In every case, where the principal obligor is relieved, the guarantor is relieved also. Therefore, the only material fact in disposing of learned counsel's argument is the fact that the Associated Oil Company was discharged, and it is perfectly immaterial whether defendant in error rendered performance impossible or whether the Associated was discharged for other reasons. Even defendant in error admits that the Associated Oil Company was relieved of liability and that admission alone requires a reversal of the judgment.

C. "Performance by the Associated Was Prevented by Strangers to the Contract, and Hence the Failure to Perform Is Not Excusable."

Defendant in error argues that performance was prevented by strangers and that hence plaintiff in error is not relieved. This argument has no application because the principal obligation expressly provided that possession must be given to the Associated Oil Company. Possession was not given and the Associated Oil Company was relieved. The rule of law invoked by learned counsel has no application.

It is thus apparent that defendant in error has failed to overcome the first obstacle. The three argu-

ments offered are all without merit. The fact that the principal obligor is admitted to have been discharged disposes of this case.

II. ALTHOUGH SOME AUTHORITIES INDICATE THAT A COMPLAINT FOR LIQUIDATED DAMAGES NEED NOT ALLEGE THE AMOUNT OF ACTUAL DAMAGE, THEY DO NOT GO SO FAR AS TO DISPENSE WITH PROOF OF SOME DAMAGE WHERE IT IS ALLEGED IN THE ANSWER THAT NO DAMAGE OCCURRED.

The answer alleges that defendant in error sustained no damage at all (Trans. Rec. p. 11). The demurrer to the answer admits this fact. For the purposes of this review, it must be taken just as though the fact were proved after trial and found as a fact.

Defendant in error misconstrues our answer where it states (Brief for Defendant in Error, p. 10):

> "In his answer defendant claimed that plaintiff was not entitled to the stipulated damages because wells drilled in the vicinity after the contract in suit was executed showed that there was no oil on the premises in question."

Our answer denies unequivocally that defendant in error sustained any damage at all and the denial is not limited or qualified in any way (Trans. Rec. p. 11).

Learned counsel also misconstrues the decision in *Sun Publishing Company v. Moore,* 183 U. S. 642; 46 L. ed. 366.

That decision is not in any way in conflict with *Northwestern Fixture Co. v. Kilbourne,* 128 Fed. 256, decided by this Honorable Court and cited in the Opening Brief for Plaintiff in Error. In the *Sun Publishing Co.* case, defendant attempted to show what the actual damages were, which is immaterial under all the authorities. Plaintiff in error here does not offer to show what the actual damages were —we set up in defense that there was absolutely no damage at all. We admit that if it be conceded to be a proper case for liquidated damages, that the actual amount of damages sustained is immaterial, but we earnestly urge that under well settled authorities which do not constitute a minority rule, that recovery cannot be had when no damage at all has been suffered.

In the case of

Bosch Magneto Co. v. Rushmore, 255 Fed. 465,

the question was not involved in any way.

In the case of

Wood v. Niagara Falls Paper Co., 121 Fed. 818,

the court intimated that in a close case the fact of no damage should incline the court to construe the contract as for a penalty rather than liquidated damages. The court was dealing with a clear case, however, for which reason it did not so construe the contract.

The decision of *Wood v. Niagara Falls Paper Co.,* supra, is apparently in conflict with the rule of this Circuit, as stated in *Northwestern Fixture Co. v. Kilbourne,* supra, but we know of no reason for referring to the rule of this Circuit as the minority rule, and it was certainly not repudiated by the Supreme Court of the United States in the *Sun Publishing Co.* case.

The reason of the rule of liquidated damages clearly shows the fallacy of learned counsel's argument.

Stipulated damages presupposes that the plaintiff has actually suffered substantial damages but that there is difficulty in measuring the *amount* thereof. Damage being admitted, the law for convenience permits the parties to stipulate an arbitrary amount rather than resort to the ordinary rules applicable.

But where there is no damage, rules of measuring damages are inapplicable and so are substitutes for those rules. There can be no difficulty in measuring damage when there is no damage. The rule dispensing with proof of the amount of damage does not obviate the necessity of showing that damage was actually suffered when the issue is properly raised.

III. THE ALLEGATION CONTAINED IN THE ANSWER THAT THE ASSOCIATED OIL COMPANY WAS BARRED BY UNAVOIDABLE DELAYS, CONSTITUTES A DEFENSE TO THE CAUSE OF ACTION PLEADED.

The Associated-Hopewell agreement provided (Trans. Rec. p. 21):

> "3. Said party of the second part * * * shall within sixty days from the date hereof place on said lands drilling materials, and shall begin actual drilling of an oil well thereon on or before the 15th day of June, A. D. 1919, with a rig capable of reaching a depth of four thousand (4000) feet, and shall prosecute the work of drilling said well continuously thereafter, *barring unavoidable delays,* until such well shall reach the depth of and test out the known productive oil sands in the Lance Creek oil field, unless oil in commercial quantities shall be found in said well at less depth."

The guaranty sued upon provides (Trans. Rec. p. 3):

> " * * * the undersigned hereby *guarantees* that the said Associated Oil Company, or its assigns, will drill and complete a well on said last above-described premises commencing on or before the 15th day of June, 1919, with a rig capable of reaching a depth of four thousand (4000) feet, and shall prosecute the well continuously thereafter, *barring unavoidable delays,* until such well shall reach the depth of and test out the known productive oil sands in the Lance Creek Field, unless oil in commercial quantities shall be found in said well at a lesser depth. * * * "

The complaint fails to allege that the Associated Oil Company was not barred by unavoidable delays, for which reason we believe it fails to state a cause of action. That becomes unimportant, however, because the answer expressly alleges (Trans. Rec. p. 10):

> " * * * that said Associated Oil Company was barred by delays unavoidable on its part,

> from drilling or commencing to drill a well on said premises, on or before said 15th day of June, 1919."

Not only the principal obligation, but the contract here sued upon both contain the limitation "barring unavoidable delays". If the default set up by defendant in error comes within the limitation, it is of course a perfect defense to the cause of action alleged.

Defendant in error meets this difficulty as follows (Brief for Defendant in Error, p. 19):

> "In the first place there is no provision in the contract excusing a failure to commence drilling by the 15th day of June, 1919. The unavoidable delay portion of the contract refers to delays after drilling had once commenced. The reason for this distinction is quite apparent because the lease between the Hopewell Oil Company and The Western States Oil and Land Company provided for a forfeiture in case drilling operations were not commenced on or before the 15th day of June, 1919. However, the above matter which plaintiff in error claims defendant in error should have alleged in its complaint *is in its nature a matter of defense.* It certainly would not be up to defendant in error to prove a negative or facts which are presumably within the sole knowledge of plaintiff in error or the Associated Oil Company."

Defendant in error argues that it is a matter in defense, apparently overlooking the fact that we did raise it as a defense and expressly set it up in our answer.

But learned counsel argues also that the words "barring unavoidable delays" do not apply to a failure to commence drilling but only to a failure to continue drilling. The question therefore is: Does the phrase "barring unavoidable delays" in the contract of guaranty modify the immediately preceding clause alone, or does it modify all of the similar, preceding clauses dealing with the same general subject?

The court will of course apply to this problem all of the well known rules applicable to the construction of contracts. No reason suggests itself to plaintiff in error, however, to give the phrase the restricted scope which defendant in error would wish. It follows alike all of those phrases specifying the things which the Associated Oil Company was to do; following it come provisions of a different character. No reason of sense suggests itself as to why plaintiff in error should require more protection against unavoidable delays after drilling had commenced than before. Learned opposing counsel says the reason is apparent—that the original lease provided for a forfeiture in case drilling was not commenced by June 15th, 1919. We are unable to see how this circumstance affects the situation. We are not construing the principal obligation but the guaranty, and Rispin would not be more likely to take the chance of having to pay $10,000 because of circumstances out of the control of the principal obligor in one case than he would in the other.

This defense has a twofold effect. It is a defense to plaintiff in error under an explicit limitation in the guaranty and is also an indirect defense as showing a discharge of the principal obligor. We submit that it raises a material issue that must be disposed of before judgment can be rendered.

IV. PLAINTIFF IN ERROR IS ENTITLED TO HAVE THE QUESTION OF THE PROPRIETY OF LIQUIDATED DAMAGES TRIED AS AN ISSUE OF FACT.

Plaintiff in error denied that damages would be impracticable or extremely difficult to fix and alleged that damages could be very easily fixed. The demurrer to the answer admits these facts. It being thus admitted that liquidated damages are unwarranted by law, can the judgment be affirmed?

This question does not arise upon demurrer to the complaint. It is not a mere question of pleading to ascertain whether from a given state of facts it follows as a conclusion of law that the damages necessarily would be difficult to fix. This question arises as an affirmative defense to which a demurrer has been interposed and which has been made the basis of a judgment. It is exactly as though the fact were proved after trial and a finding to that effect made by the court.

Decisions of courts which merely pass upon the sufficiency of complaints and which merely decide

the necessity of alleging the difficulty of fixing damages, are not necessarily in point. It is one thing to say that one need not allege the difficulty of fixing damages and quite another to say that plaintiff could still recover although the contrary clearly appeared. The decisions must be examined keeping this distinction in mind and the language of courts must be construed in the light of how the question was presented.

Defendant in error submits no authority against our position which is in point. In

McComber v. Kellerman, 162 Cal. 749,

cited by learned counsel, it appeared by *proof* that the case was a proper one for liquidated damages. The court never said or intimated in its opinion, that if it had appeared by proof that it was *not* a proper case for liquidated damages that plaintiff could still recover. And in the case at bar, it must be assumed to be *proved* that it is not a proper case for liquidated damages.

In

Escondido Oil Co. v. Glaser, 144 Cal. 494,

we have a similar situation. The question arose on demurrer to the complaint. The court never said that even though it affirmatively appear that it is an improper case for liquidated damages, plaintiff could still recover. It merely decided that on the facts of that particular case it was not necessary to allege that the damages were difficult to fix.

And similarly in

Blodget v. Columbia Live Stock Co., 164 Fed. 305,

decided by this Honorable Court and cited by defendant in error. It did not there appear that it was *not* difficult or impracticable to fix the damages and indeed, the trial court found as a fact that the actual damages could *not* be determined. Judge Ross certainly never said that even if it appeared that actual damages were easy to ascertain that liquidated damages would nevertheless be given.

We must disagree also with learned counsel's reading of

Dyer v. Central Iron Works, 182 Cal. 588.

The court there certainly did say that the complaint would have been defective in the absence of an allegation that damages would be difficult to fix. That is not important, however, because plaintiff in error concedes that from certain facts it may well follow as a conclusion of law that damages would be difficult to ascertain. But neither the Supreme Court of California, nor this Honorable Court, nor any other so far as the writer is aware, has ever decided or even intimated that liquidated damages could ever be upheld in a case where it was clearly established by both pleading and proof that damages were not difficult or impracticable to fix. And the demurrer to the answer in the case at bar admits those facts.

There is a possible answer to our contention which learned opposing counsel does not suggest, but which will readily occur to the court, namely this: In a case where it follows as a conclusion of law from the facts pleaded that damages are difficult to fix, can the defendant put the propriety of liquidated damages in issue without denying the facts? In such case, is not a denial that damages are difficult to fix, a mere conclusion of law which cannot stand against the admitted facts? The answer is very clear. Difficulty of fixing damages must be alleged where the difficulty is not obvious. Where the difficulty is obvious, it need not be alleged. But precisely as the difficulty may really exist in cases where common experience would not lead one to suspect it, so also it may not really exist in cases where common experience would lead one to suspect that it did. In the former contingency, the pleader need only allege the fact that damages are difficult to fix in order to secure his day in court upon that issue. Is it possible to suggest a valid reason why in the latter contingency the pleader may not have his day in court by denying the fact?

V. THE CONTRACT IN THIS CASE PROVIDES FOR A PENALTY AND NOT FOR LIQUIDATED DAMAGES. A GUARANTY IS ALWAYS PENAL AND CANNOT PROVIDE FOR LIQUIDATED DAMAGES.

In our opening brief we set forth all of the tests known to the law for determining whether a con-

tract provides for a penalty or for liquidated damages, and demonstrated how the contract herein meets all the requirements of a penalty and fails to meet any of the tests of liquidated damages. Defendant in error replies with great brevity and cites a single decision culled from our own opening brief.

We have argued that if a gross sum is stipulated to be paid for any failure to fulfill an agreement consisting of several parts, and the sum is payable for a breach of any one of them, that the sum stipulated is a penalty. On page 15 of our opening brief and following we cite numerous authorities. The case of *Escondido Oil Company v. Glasier,* cited by defendant in error, is in line with the other authorities cited by plaintiff in error, and we ourselves cite it and explain it in our opening brief. Defendant in error does not cite a single decision holding contrary to the decisions cited on pages 15 and 16 of our opening brief. The rule is applied by all courts everywhere.

Defendant in error offers but one possible answer to these authorities. Learned counsel says it is apparent that the contract does not contain a number of separate covenants of varying degrees of importance, for the breach of any one of which plaintiff in error would be liable in the sum of $10,000.00. Plaintiff in error respectfully refers the court to page 17 of its opening brief, on which page are listed some of the diverse acts for the performance of every one of which plaintiff in error was bound in

the sum of $10,000.00. Defendant in error ignores this categorical demonstration. Its correctness cannot be disputed and it places the contract in this case on all fours with the leading cases cited in our brief.

Even the cases cited by defendant in error say that where the disparity is great between the actual damage and the stipulated sum, that the courts should incline to construe the provision as for a penalty, and in the case at bar the disparity is admitted to be the disparity between zero and $10,000.00.

To our argument that collateral agreements are always construed to be penalties, defendant in error likewise has to admit the correctness of the rule and rest his case on a denial of the fact. To deny that the contract involved in this case is collateral is to lean against a very slight reed, however. Every contract of guaranty is collateral. Every text, encyclopedia and decision so defines it. What else could a secondary obligation be but collateral?

We confidently assert that it is impossible in law to stipulate damages at all in a contract of guaranty. We have never seen a case where such a thing has been upheld. All courts hold that damages cannot be stipulated at all in collateral agreements. To permit damages to be stipulated in a guaranty contract is to license gambling. A guaranty is always penal and recovery is always limited to the damages actually sustained.

It is one thing to say that you can stipulate damages with the person who has to perform the contract and quite another thing to say you can do so with a stranger. The Associated Oil Company might do so because it was obligated to do the act and defendant in error might do so because it was entitled to performance, but as to an outsider like plaintiff in error, the performance or non-performance of the contract is a mere arbitrary event over which he has no control.

We respectfully submit that under well settled principles of law the contract here sued upon provides for a penalty and not for liquidated damages. Not only the nature of the provision but the character of the contract compels this construction.

VI. CONCLUSION.

The requirements of substantial justice in this case are easily perceptible in the record. Defendant in error, with mock seriousness, wails that it paid dearly for this contract and is entitled to the $10,000.00.

But defendant in error did not dismiss its lawsuit in consideration of $10,000.00. It dismissed it in consideration of a secondary obligation on the part of plaintiff in error—an obligation which it was contemplated and intended by the parties should be discharged by the mere performance of its contract on the part of the Associated Oil Company. De-

fendant in error well knew and fully appreciated that when the Associated performed its contract, plaintiff in error was to be discharged without the payment of a single solitary cent. To say that defendant in error dismissed its suit for $10,000.00 and that now we will not pay the money is not a fair statement of what this record shows. Defendant in error dismissed its suit in exchange for what it hoped was a valuable piece of oil land, which would be tested without a cent of cost to it by a responsible party, and for a secondary obligation, well knowing its collateral character and that plaintiff in error would in all probability be discharged without the payment of the penalty.

Therefore, upon the record in this case, defendant in error has already received in full the very utmost which it bargained for. As learned counsel points out in his brief (page 14) the entire object of the contract was to insure that the Associated Oil Company would perform its contract and learned counsel himself concedes that the Associated Oil Company did not default.

Defendant in error was anxious and willing to dismiss its lawsuit in exchange for a gamble on a piece of oil land. It did not ask plaintiff in error for any money but only to stand behind the Associated Oil Company. Defendant in error received its oil land; the Associated did its best to perform its contract and defendant in error had its gamble and lost. That the land has been demonstrated to be

of no value for oil gives the motive but not a cause for mulcting plaintiff in error of $10,000.00.

Plaintiff in error has already concluded its argument on the law as we understand it, but in so far as mere abstract principles of fairness and justice may have a place in the determination hereof, we respectfully submit that defendant in error has assumed an unconscionable position and is urging a claim of great unfairness.

Respectfully submitted,

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Dated, San Francisco,
July 18, 1923.